LIBRARY
SUPREME COURT, U. S.

Supreme Court, U. S.
FILED
OCT 29 1973
MICHAEL RODAK, JR., CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. 73-699

ROBERT E. LEE, ... Petitioner

v.

SECURITIES AND
EXCHANGE COMMISSION, ... Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

CHARLES V. BOARMAN
HENDERSON, BOARMAN
& OEXMANN
179 North Upper Street
Lexington, Kentucky 40507
Counsel for Petitioner

PROFESSIONAL PRINTING CO., 1113 Commercial Dr., Lexington, Ky. 40505 - 252-3602

INDEX

Page

Opinion Below 1

Jurisdiction 2

The Questions Presented for Review 2-4

The Statutes and Regulations Which the Case Involves 4-6

Statement of the Case 6-12

Reasons for Granting Certiorari 13-14

Appendix A — Opinion and Judgment of Court of Appeals 1a-9a

Appendix B — Findings of Fact and Conclusions of Law of District Court 10a-17a

Appendix C — Final Judgment of District Court 18a-21a

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. _____

ROBERT E. LEE, ... Petitioner

v.

SECURITIES AND
EXCHANGE COMMISSION, ... Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

The Petitioner, Robert E. Lee, respectfully prays that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Sixth Circuit entered in the proceeding on July 31, 1973.

OPINION BELOW

The Opinion of the Court of Appeals, not yet reported, appears in the Appendix hereto. The Opinion of the District Court for the Eastern District of Kentucky is reported in ..... F. Supp. .....

JURISDICTION

The judgment of the Court of Appeals for the Sixth Circuit was entered on July 31, 1973, and this Petition for Certiorari was filed within ninety days of that date. This Court's jurisdiction is invoked under 28 U.S.C. 1254. No order has been entered respecting any rehearing and no extension of the time in which to petition for Writ of Certiorari has been sought.

The United States District Court for the Eastern District of Kentucky had jurisdiction of this action under Section 22(a) of the Securities Act of 1933 (15 U.S.C. 77v(a)) and Section 27 of the Securities Exchange Act of 1934 (15 U.S.C. 78aa).

THE QUESTIONS PRESENTED FOR REVIEW

1. Whether Petitioner, who provided such clerical services to a corporation as preparing drafts of various documents, participating in board of directors' discussions, drafting resolutions of the board of directors; and who received for his attendance at board meetings the same amount as directors ($15.00 per meeting), was responsible for the actions of the corporation and subject to injunctive relief under the provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934 and regulations promulgated under the latter.

2. Whether Petitioner was, under the law, a member of the executive committee of a Kentucky

corporation by way of appointment thereto where the applicable state statute provided that only a member of the board of directors could be elected to the executive committee of a Kentucky corporation.

3. Whether Petitioner as a member of a management company which had contracted to furnish certain management services to a corporation was liable under the Securities Act of 1933 and the Securities Exchange Act of 1934 and regulations promulgated under the latter for the acts or omissions of the hiring corporation where the officers and directors of the hiring corporation remained in office and continued to function as such.

4. Whether Petitioner was liable under the Securities Act of 1933 and the Securities Exchange Act of 1934 and regulations promulgated thereunder for having led discussions at an annual shareholders meeting and directors meeting during the course of which meeting neither he nor anyone else discussed or disclosed certain financial problems being experienced by the corporation where Petitioner was not an officer or director of the corporation.

5. Whether the Petitioner is liable under the Securities Act of 1933 and the Securities Exchange Act of 1934 and regulations promulgated under the latter for the preparation of a registration statement and prospectus for a subsidiary corporation where only a small quantity of the issued stock was sold, the registration was withdrawn and all monies raised, including commissions, were returned to the purchasers.

6. Should the District Court have dismissed this action when Petitioner moved the Court to do so?

THE STATUTES AND REGULATIONS WHICH THE CASE INVOLVES

The case involves claimed violations of Section 17(a) of the Securities Act of 1933, as amended (15 U.S.C. 77q(a)): and Section 10(b) and Rule 10b-5) thereunder of the Securities Exchange Act of 1934, as amended (15 U.S.C. 78j (6)) and (17 C.F.R. 240.10 (b-5)): and KRS 271.345(4)(d). The texts of the foregoing statutes and regulation are set out verbatim as follows:-

Section 17(q) of Securities Act of 1933

(a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly —

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or

would operate as a fraud or deceit upon the purchaser.

Section 10(b) of Securities Exchange Act of 1934

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors. June 6, 1934, c. 404, § 10, 48 Stat. 891.

Rule 10 (b-5)

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

KRS 271.345(4)(d)

The board of directors may, by resolution passed by a majority of the whole board, designate two or more of their number to constitute an executive committee, who, to the extent provided in the resolution, shall have and exercise the authority of the board of directors in the management of the corporation.

STATEMENT OF THE CASE

On March 1, 1971, the Securities and Exchange Commision brought an action in the United States District Court for the Eastern District of Kentucky against Petitioner Robert E. Lee and others, seeking issuance of an injunction against the defendants in that action prohibiting them from committing certain violations of the anti-fraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934 and the regulations promulgated under the latter. The corporate defendants defaulted, and all individual defendants except Petitioner Robert E. Lee consented to the entry of orders of injunction against them. A two-day trial was held at Lexington, Kentucky, at the conclusion of which the Court made certain findings of fact and conclusions of law and issued and filed an injunction against Petitioner Robert E. Lee as

prayed for in the complaint Petitioner then prosecuted an appeal to the United States Court of Appeals for the Sixth Circuit and on July 31, 1973, the U. S. Court of Appeals rendered a decision affirming the District Court. The opinion of the Court of Appeals, not yet reported, appears in the appendix hereto.

In its opinion, the Court of Appeals set out certain findings of fact upon the basis of which that Court affirmed the District Court. The findings can be broken down into a small number of categories related to Petitioner's duties and job experience as an employee of American Associated Systems, Inc., a Kentucky corporation. While the full opinion is set out in the appendix, the categories of findings can be summarized as follows:

(1) Drafting of Documents

That Petitioner, not as an officer or director of the company, prepared agendas for directors meetings, drafted resolutions and drafted a misleading quarterly report to stockholders and prepared a misleading registration statement and prospectus for another corporation, American Associated Financial Corporation.

(2) Participation In Discussions

The Court of Appeals found that Petitioner had led board of directors' discussions with relation to the business of American Associated Systems, Inc. and that while attending the 1970 annual shareholders and

directors meeting, Petitioner failed to disclose certain financial problems being experienced by the company.

(3) Apparent Holding Of A Management Position

That Petitioner was "paid as a director"; and that he served for a time on the executive committee of American Associated Systems, Inc., and "owned" a management company which had a management contract with American Associated Systems, Inc.

As shown by the transcript, Petitioner is an attorney at law, licensed in the State of Tennessee. From the year 1967, Petitioner, while employed by a corporation totally unrelated to American Associated Systems, Inc., a Kentucky corporation, gratuitously gave his time and advice at irregular intervals to Mr. Joel Jackson and others who were concerned with the organization of American Associated Systems, Inc. (Petitioner's employer was compensated for some of his efforts.) Petitioner prepared the draft of a registration statement and prospectus for a public issue of stock for American Associated Systems, Inc. and later for a subsidiary called Belva Manor, Inc. and another subsidiary named American Associated Financial Corporation, all Kentucky corporations. The registration statements and prospecti were prepared for the signature of and signed by an attorney other than Petitioner. Petitioner became an employee of American Associated Systems, Inc. on January 1, 1970. By this time the primary offerings of stock in American

Associated Systems, Inc. and Belva Manor, Inc. had been sold in their entirety. The American Associated Financial Corporation issue was offered to the public subsequent to the commencement of Petitioner's employment with the parent company, but the registration was withdrawn in its early stages and all funds raised as a result of the issue, including commissions, were refunded in full. Petitioner's principal duties with American Associated Systems, Inc. from January 1, 1970 until he was summarily dismissed on August 8, 1970, consisted of drafting of various documents, putting the company's numerous files in order and generally advising the management in his capacity as house counsel.

Both the District Court and the Court of Appeals, in finding that Petitioner did considerable drafting of agendas, minutes, resolutions and of registrations and prospecti, seemed to have detemined that Petitioner was in the position of an officer or director of the company, that he was in a decision-making position with the company and that his decision-making and policy-making powers, when exercised, caused or contributed to the financial failure of the company. Likewise, both the District Court and the Court of Appeals seemed to have taken the view that because Petitioner was prominent in the discussions carried on by the directors of the company, his involvement in these discussions caused or contributed to the financial failure of the company. A point importantly relied on by both courts below is that Petitioner was paid the same amount of money for attending board meetings as

was paid to the board members themselves, i.e., $15.00 per meeting.

It is indisputable that Joel S. Jackson was the president of American Associated Systems, Inc. and that Petitioner was neither an officer nor a director of the company, but that he served as house counsel or "chief corporate counsel" from January 1, to August 8, 1970. Prior to January 1, 1970, Petitioner had no position of employment with the company at all. The courts have seemed to attach to the job of drafting documents the presumption that the drafter was in a decision-making or policy-making position with the company. To the contrary, the record shows that the decision-making function of the company was exercised by Joel Jackson, the president, and that the task of Petitioner was to *put into words*, by way of minutes, resolutions, etc., the decisions and policies of the company reached by management. The preparation of an agenda for a directors meeting does not require policy-making or decision-making powers in the writer. Such a task could be adequately done by an ordinary clerical employee. That Petitioner was involved in or led discussions at meetings of the board of directors or of the stockholders of the company was a normal consequence of his position as counsel. First, in his position as a friend of the company regularly invited to meetings of the directors, and later as house counsel to expect that he would refuse to be a party to conversations or discussions related to the field of his training would be unusual. The fact that as an attorney he was willing to discuss with management

any legal problems faced by management does not imply that legal counsel was himself a member of management. When management sought counsel's advice before making executive decisions, it was necessary for management to be frank and open with counsel in seeking advice. It goes without saying, however, that offering advice concerning the *legal alternatives* open to a company does not constitute making executive decisions. If Petitioner failed at any time to state any facts concerning the company, either to the stockholders or to the management, or to others, this was because, as the transcript shows, Petitioner was in a position of taking orders and not giving them; he was in a position of advising management in carrying out its policies, but not in making the policies themselves.

While Petitioner was a stockholder of a management company which contracted for a short time to provide certain management services to American Associated Systems, Inc., the management contract entered into could not and did not purport to diminish the powers or responsibilities of the elected officers and directors of the company. Even as an employee of the management company, Petitioner had no position with relation to American Associated Systems, Inc. which was different from his prior relationship as counsel.

Finally, as would be apparent from the transcript, Plaintiff, Securities and Exchange Commission filed a sworn complaint in the District Court stating that Petitioner Robert E. Lee had been a director of American Associated Systems, Inc. This allegation was

rescinded by the Securities and Exchange Commission in the course of the trial. Respondent could have discovered, as a result of simple pre-trial investigative procedures, that Petitioner had never been a director of the company. The fact that the false allegation had been made, and was not rescinded at the outset, prejudiced the Petitioner in the view of the Court, and necessitated his using a great deal of the Court's time to prove a negative fact — that he had not been an officer or director of the company — by cross examination of virtually all of Respondents witnesses. This action is an equitable action, and the doctrine still applies that a plaintiff in equity must come into equity with clean hands. The District Court should have dismissed the action at the trial when Petitioner moved the Court to do so.

The transcript shows throughout that, in connection with the business of American Associated Systems, Inc., Petitioner consistently cautioned the company's management, in vain, against taking several courses that would prove to be undesirable; that he was a vigorous advocate of full disclosure of information to everyone concerned; that he attempted to put the company's records in order; and that, even after he had been summarily dismissed from his employment, he offered to assist the board of directors in restructuring and refinancing the company's trouble-ridden construction projects.

REASONS FOR GRANTING CERTIORARI

The Court of Appeals was in error in imputing to Petitioner the responsibility for acts or omissions of American Associated Systems, Inc. in the face of the words and tenor of the transcript of the trial. Witnesses for the Securities and Exchange Commission testified uniformly that Petitioner was neither an officer nor a director of the company, but that he was counsel to the company. Many of the duties which he performed were simple secretarial tasks. He drafted documents in reliance on information supplied to him by the president of the company, by the company's accountant, by a banker on the board, and by others possessing knowledge more intimate than his own. His was, perhaps, the chief voice among company employees in calling for fairness, openness and full disclosure of facts. By the limited means available to him he attempted to influence the company's management to take the safe course demanded by the very statutes and regulation under which this action was brought. That the company hired Petitioner in order to take advantage of his familiarity with securities law and then failed to follow his advice, was unfair. The Court's finding against him was a result of a misinterpretation of the applicable statutes and regulation with relation to the facts. In finding Petitioner liable, the Court is imputing to him power which he did not possess, and blaming him for a series of occurrences which he was powerless to stop. If such a precedent should remain in effect, the anti-fraud

statutes will have application far beyond their intended reach. No longer will the possession of corporate power, and the wrongful exercise of the same, be punishable alone. Instead, those without the power to change anything will be equally punishable.

For these reasons, a Writ of Certiorari should issue to review the Judgment and Opinion of the Court of Appeals for the Sixth Circuit.

Respectfully submitted,

CHARLES V. BOARMAN
HENDERSON, BOARMAN & OEXMANN
179 North Upper Street
Lexington, Kentucky 40507
Counsel for Petitioner

APPENDIX A

Nos. 73-1064 and 73-1065

UNITED STATES COURT OF APPEALS
For The Sixth Circuit

SECURITIES AND EXCHANGE COMMISSION, ... Appellee,

v.

AMERICAN ASSOCIATED SYSTEMS, INC., ET AL.,
ROBERT EDWIN LEE, ... Appellant.

Appeal from the United States District Court
For the Eastern District of Kentucky

Decided and Filed July 31, 1973

Before: Phillips, Chief Judge, Celebrezze and Peck, Circuit Judges.

Per Curiam. Defendant-appellant, Robert E. Lee, seeks reversal of an order for permanent injunction entered against him. The injunction forbids further violations of the anti-fraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934. We affirm.

This action, brought by the Securities Exchange Commission, originally sought permanent injunctions against three Kentucky corporations and eight individuals. Default judgments were entered against

the corporate defendants and permanent injunctions by consent were entered against each of the individual defendants, except Lee. The findings of fact and conclusions of law of District Judge Mac Swinford are attached as an appendix to this opinion.

The trial record reveals that Lee, as corporate counsel for American Associated Systems, Inc. (AASI), prepared board of directors' meeting agendas, led board discussions, drafted resolutions and was paid as a director. He served also as a member of AASI's executive committee and owned the management corporation which managed AASI and its subsidiaries.

In 1970, when AASI was experiencing serious cash-flow problems and Lee was aware of these problems, he prepared a quarterly report for AASI which failed to disclose the difficulties. Also included in this report were false statements concerning Belva Manor, as AASI subsidiary which had diverted funds intended for construction of a nursing home to other purposes.

Lee failed also to disclose the financial problems of AASI at the 1970 annual shareholders' meeting and the directors' meeting immediately thereafter. He led discussions at both meetings. Appellant also prepared a misleading registration statement and prospectus for American Associated Financial Corp., another AASI subsidiary.

A careful review of the record reveals substantial

support for the District Court's findings and conclusions.

Affirmed.

APPENDIX

FINDING OF FACT AND CONCLUSIONS OF LAW

This cause coming on to be heard on motion of Plaintiff, Securities and Exchange Commission, for a judgment of permanent injunction in accordance with the Complaint filed herewith as to defendant Robert E. Lee and the Court having considered the Complaint and the Answer of the defendant and having heard evidence and arguments of counsel, the Court makes Findings of Fact and Conclusions of Law, as follows:

FINDINGS OF FACT

1. That American Associated Systems, Inc. is a Kentucky corporation which was organized on May 29, 1967 as Educational Funds, Inc. The name was changed to American Associated Systems, Inc. on July 24, 1969.

2. That Belva Manor, Inc. is a Kentucky corporation which was acquired by Education Funds, Inc. on June 19, 1969.

3. That American Associated Financial Corporation is a Kentucky corporation which was organized on March 3, 1970.

4. That between August 1969 and December 1969, Belva Manor, Inc. had a public offering of 450,000 shares of its common stock at $2 per share. The use of the mails was utilized.

5. That approximately 1,000 persons paid $900,000 for the shares of stock offered by Belva Manor, Inc.

6. That the prospectus furnished to purchasers of the securities of Belva Manor stated that Belva Manor had $100,000 on deposit with the Corbin Deposit Bank of Corbin, Kentucky. This statement was, in fact, false.

7. That the Belva Manor, Inc. prospectus stated that the proceeds from the sale of the public offering were to be utilized for the construction of a nursing home.

8. That, in fact, prior to the completion of the offering by Belva Manor, Inc., in December 1969, monies from the public offering were being utilized for the operations of American Associated Systems, Inc., an affiliate corporation of Belva Manor, Inc., as well as for subsidiaries of American Associated Systems, Inc. and by corporations owned and controlled by officers and directors of Belva Manor, Inc.

9. That Associated Management Corporation was organized under the laws of Kentucky in 1970 and was owned equally by Robert E. Lee, Joel S. Jackson, William E. Bohon, and Alvin L. Norton. Associated Management Corporation was organized

to provide managerial, legal, and accounting services to American Associated Systems, Inc., as well as its subsidiaries and affiliates, commencing January 1, 1970 and it was to be paid $150,000 annually for such services. These services were to be provided by Robert E. Lee, William E. Bohon, Joel S. Jackson, and Alvin L. Norton. Each individual was to be paid, and was paid, $3,000 per month.

10. That Hester Finance Co., Inc. was acquired by American Associated Systems, Inc. on January 31, 1970 for 15,000 shares of the latter corporation's stock. Associated Investors was the principal shareholder of Hester Finance Co. prior to its acquisition by American Associated Systems, Inc. Lee owned 40,000 shares of Associated Investors stock both prior and subsequent to January 31, 1970. Two loans, totalling $25,000, were granted to Hester Finance Co. during November and December 1969. These were not disclosed in the "Plan of Reorganization" dated January 31, 1970 between American Associated Systems, Inc. and Hester Finance Co.

11. That Robert E. Lee attended almost all of the directors meetings of American Associated Systems, Inc., its subsidiaries and affiliates, from 1967 through August 1970. Corporate minutes of American Associated Systems, Inc. provided that Lee was to be compensated at the same rate as the other directors for his attendance at the meetings of the board of directors. Lee prepared agendas, presented matters to the board, proposed resolutions, and kept and maintained the corporate minute books for all of the entities.

12. That as of January 1970, Lee had knowledge of the fact that the monies obtained from the offer and sale of the common stock of Belva Manor, Inc. to the public had been misappropriated and utilized for purposes other than that which was specified in the registration statement filed with the Commonwealth of Kentucky and prospectus furnished to the purchasers of said securities.

13. That a board of directors meeting for Belva Manor, Inc. was held on February 21, 1970. The agenda of said meeting was prepared by Robert E. Lee. The board of directors was requested to authorize and approve the making of a loan of $722,295.07 to American Associated Systems, Inc. in order to permit the latter corporation to reduce its outstanding bank loans. The directors, who were not also officers, were not advised or apprised of the fact that the monies had already been expended as is indicated in Finding 8. It was further represented to the board of directors at said meeting that Belva Manor, Inc. would be furnished notes representing said loans and these notes would be fully secured. No notes representing said loans were ever made or delivered, nor were said loans secured.

14. That in April and May 1970, American Associated Systems, Inc., and its subsidiaries were experiencing cash flow problems. At this time, Lee was being furnished with daily schedules of bank balances for American Associated Systems, Inc., and its subsidiaries.

15. That Lee prepared the American Associated Systems, Inc., Third Quarter Report — 1970 which was mailed to all the shareholders of American Associated Systems, Inc., in about May of 1970. Said report did not disclose any of the cash flow problems being experienced by American Associated Systems, Inc., or its subsidiaries. The report also stated that the funds of Belva Manor had been invested in short-term paper. This statement was false in fact. No disclosure was made by Lee that the funds had been utilized by corporations which were owned and controlled by officers and directors of Belva Manor nor was any disclosure made that any loans had been made to Associated Management Corporation which was owned and controlled by Lee, Bohon, Norton, and Jackson.

16. That a shareholders meeting was held in June 1970 of American Associated Systems, Inc. Lee presented the agenda and led the discussions. Lee stated at the shareholders meeting that the company was experiencing no financial difficulties. He failed to disclose the cash flow problems which the company was then experiencing.

17. That Lee, in May of 1970, had knowledge concerning the cash flow difficulties which American Associated Systems, Inc., and its subsidiaries were experiencing. Richard Stoy was requested to join the company as a financial administrator. Lee discussed the cash flow problems with Stoy and stated that the difficulties would be alleviated by a new public offer-

ing to be made by a subsidiary of American Associated Systems, Inc., American Associated Financial Corp.

18. That Lee prepared the registration statement and prospectus for American Associated Financial Corporation. The prospectus is dated July 15, 1970. Four hundred thousand (400,000) shares of its common stock were offered to the public at $2 per share. The prospectus failed to disclose the financial difficulties being experienced by American Associated Systems, Inc. and its subsidiaries. It also did not disclose that the funds from the Belva Manor offering had been utilized by American Associated Systems, Inc. for purposes other than those stated in the Belva Manor prospectus or by corporations owned and controlled personally by officers and directors of Belva Manor, Inc.

19. That Lee offered and sold 1,250 shares of common stock of American Associated Systems, Inc. in May, 1970 through an agent. The agent was only told that Lee needed money. Lee failed to disclose any of the financial difficulties being experienced by American Associated Systems, Inc. and its subsidiaries nor did he disclose that funds of Belva Manor, Inc. had been misappropriated. Lee received approximately $2,500 plus stock of another corporation as the proceeds from the sale of his stock.

CONCLUSIONS OF LAW

For the foregoing facts, the Court adopts the following Conclusions of Law:

1. That this Court has jurisdiction of this action under Section 22(a) of the Securities Act of 1933, as amended, (15 U.S.C. 77v(a)) and Section 27 of the Securities Exchange Act of 1934, as amended, (15 U.S.C. 78aa), and that it has jurisdiction of the defendant.

2. That the defendant has violated Section 17(a) of the Securities Act of 1933 (15 U.S.C. 77q(a)) and Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78j(b)) and Rule 10b-5 promulgated thereunder (17 C.F.R. 240.10b-5).

3. That a final judgment of permanent injunction should be granted in accordance with the Plaintiff's motion.

Dated this 31st day of July, 1972.

ENTER:

MAC SWINFORD
United States
District Court Judge

* * * * * * *

APPENDIX B

IN THE DISTRICT COURT
OF THE UNITED STATES
EASTERN DISTRICT OF KENTUCKY
AT LEXINGTON

SECURITIES AND
EXCHANGE COMMISSION, ... Plaintiff

v.

AMERICAN ASSOCIATED
SYSTEMS, INC.,
BELVA MANOR, INC.,
AMERICAN ASSOCIATED
FINANCIAL CORP.,
JOEL S. JACKSON,
ALVIN L. NORTON,
WILLIAM E. BOHON,
PAUL D. ROSS,
ROBERT E. LEE,
MAJ. GEN. BENJAMIN J. BUTLER,
DR. CHARLES N. TARKINGTON,
MAXWELL B. DUNCAN, SR., ... Defendants

CIVIL ACTION
FILE NO. 2243
Filed July 31, 1972

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This cause coming on to be heard on motion of Plaintiff, Securities and Exchange Commission, for

a judgment of permanent injunction in accordance with the Complaint filed herewith as to defendant Robert E. Lee and the Court having considered the Complaint and the Answer of the defendant and having heard evidence and arguments of counsel, the Court makes Findings of Fact and Conclusions of Law, as follows:

FINDINGS OF FACT

1. That American Associated Systems, Inc. is a Kentucky corporation which was organized on May 29, 1967 as Educational Funds, Inc. The name was changed to American Associated Systems, Inc. on July 24, 1969.

2. That Belva Manor, Inc. is a Kentucky corporation which was acquired by Educational Funds, Inc. on June 19, 1969.

3. That American Associated Financial Corporation is a Kentucky corporation which was organized on March 3, 1970.

4. That between August 1969 and December 1969, Belva Manor, Inc. had a public offering of 450,000 shares of its common stock at $2 per share. The use of the mails was utilized.

5. That approximately 1,000 persons paid $900,000 for the shares of stock offered by Belva Manor, Inc.

6. That the prospectus furnished to purchasers of the securities of Belva Manor stated that Belva

Manor had $100,000 on deposit with the Corbin Deposit Bank of Corbin, Kentucky. This statement was, in fact, false.

7. That the Belva Manor, Inc. prospectus stated that the proceeds from the sale of the public offering were to be utilized for the construction of a nursing home.

8. That, in fact, prior to the completion of the offering by Belva Manor, Inc., in December 1969, monies from the public offering were being utilized for the operations of American Associated Systems, Inc., an affiliate corporation of Belva Manor, Inc., as well as for subsidiaries of American Associated Systems, Inc. and by corporations owned and controlled by officers and directors of Belva Manor, Inc.

9. That Associated Management Corporation was organized under the laws of Kentucky in 1970 and was owned equally by Robert E. Lee, Joel S. Jackson, William E. Bohon, and Alvin L. Norton. Associated Management Corporation was organized to provide managerial, legal, and accounting services to American Associated Systems, Inc., as well as its subsidiaries and affiliates, commencing January 1, 1970 and it was to be paid $150,000 annually for such services. These services were to be provided by Robert E. Lee, William E. Bohon, Joel S. Jackson, and Alvin L. Norton. Each individual was to be paid, and was paid, $3,000 per month.

10. That Hester Finance Co., Inc., was acquired by American Associated Systems, Inc. on January 31,

1970 for 15,000 shares of the latter corporation's stock. Associated Investors was the principal shareholder of Hester Finance Co. prior to its acquisition by American Associated Systems, Inc. Lee owned 40,000 shares of Associated Investors stock both prior and subsequent to January 31, 1970. Two loans, totalling $25,000, were granted to Hester Finance Co. during November and December 1969. These loans were not disclosed in the "Plan of Reorganization" dated January 31, 1970 between American Associated Systems, Inc. and Hester Finance Co.

11. That Robert E. Lee attended almost all of the directors meetings of American Associated Systems, Inc., its subsidiaries and affiliates, from 1967 through August 1970. Corporate minutes of American Associated Systems, Inc. provided that Lee was to be compensated at the same rate as the other directors for his attendance at the meetings of the board of directors. Lee prepared agendas, presented matters to the board, proposed resolutions, and kept and maintained the corporate minute books for all of the entities.

12. That as of January 1970, Lee had knowledge of the fact that the monies obtained from the offer and sale of the common stock of Belva Manor, Inc. to the public had been misappropriated and utilized for purposes other than that which was specified in the registration statement filed with the Commonwealth of Kentucky and prospectus furnished to the purchasers of said securities.

13. That a board of directors meeting for Belva Manor, Inc. was held on February 21, 1970. The agenda of said meeting was prepared by Robert E. Lee. The board of directors was requested to authorize and approve the making of a loan of $722,295.07 to American Associated Systems, Inc. in order to permit the latter corporation to reduce its outstanding bank loans. The directors, who were not also officers, were not advised or apprised of the fact that the monies had already been expended as is indicated in Finding 8. It was further represented to the board of directors at said meeting that Belva Manor, Inc. would be furnished notes representing said loans and these notes would be fully secured. No notes representing said loans were ever made or delivered, nor were said loans secured.

14. That in April and May 1970, American Associated Systems, Inc., and its subsidiaries were experiencing cash flow problems. At this time, Lee was being furnished with daily schedules of bank balances for American Associated Systems, Inc., and its subsidiaries.

15. That Lee prepared the American Associated Systems, Inc., Third Quarter Report — 1970 which was mailed to all the shareholders of American Associated Systems, Inc., in about May of 1970. Said report did not disclose any of the cash flow problems being experienced by American Associated Systems, Inc., or its subsidiaries. The report also stated that the funds of Belva Manor had been invested in short-term paper. This statement was false in fact. No

disclosure was made by Lee that the funds had been utilized by corporations which were owned and controlled by officers and directors of Belva Manor nor was any disclosure made that any loans had been made to Associated Management Corporation which was owned and controlled by Lee, Bohon, Norton, and Jackson.

16. That a shareholders meeting was held in June 1970 of American Associated Systems, Inc. Lee presented the agenda and led the discussions. Lee stated at the shareholders meeting that the company was experiencing no financial difficulties. He failed to disclose the cash flow problems which the company was then experiencing.

17. That Lee, in May of 1970, had knowledge concerning the cash flow difficulties which American Associated Systems, Inc., and its subsidiaries were experiencing. Richard Stoy was requested to join the company as a financial administrator. Lee discussed the cash flow problems with Stoy and stated that the difficulties would be alleviated by a new public offering to be made by a subsidiary of American Associated Systems, Inc., American Associated Financial Corp.

18. That Lee prepared the registration statement and prospectus for American Associated Financial Corporation. The prospectus is dated July 15, 1970. Four hundred thousand (400,000) shares of its common stock were offered to the public at $2 per share. The prospectus failed to disclose the financial difficulties being experienced by American Associated Systems,

Inc. and its subsidiaries. It also did not disclose that the funds from the Belva Manor offering had been utilized by American Associated Systems, Inc. for purposes other than those stated in the Belva Manor prospectus or by corporations owned and controlled personally by officers and directors of Belva Manor, Inc.

19. That Lee offered and sold 1,250 shares of common stock of American Associated Systems, Inc. in May, 1970 through an agent. The agent was only told that Lee needed money. Lee failed to disclose any of the financial difficulties being experienced by American Associated Systems, Inc. and its subsidiaries nor did he disclose that funds of Belva Manor, Inc. had been misappropriated. Lee received approximately $2,500 plus stock of another corporation as the proceeds from the sale of his stock.

CONCLUSIONS OF LAW

From the foregoing facts, the Court adopts the following Conclusions of Law:

1. That this Court has jurisdiction of this action under Section 22(a) of the Securities Act of 1933, as amended, (15 U.S.C. 77v(a)) and Section 27 of the Securities Exchange Act of 1934, as amended, (15 U.S.C. 78aa), and that it has jurisdiction of the defendant.

2. That the defendant has violated Section 17(a) of the Securities Act of 1933 (15 U.S.C. 77q(a)) and

Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78j(b)) and Rule 10b-5 promulgated thereunder (17 C.F.R. 240.10b-5).

3. That a final judgment of permanent injunction should be granted in accordance with the Plaintiff's motion.

Dated this 31st day of July, 1972.

ENTER:

/s/ Mac Swinford
United States
District Court Judge

* * * * * * *

APPENDIX C

IN THE DISTRICT COURT
OF THE UNITED STATES
EASTERN DISTRICT OF KENTUCKY
AT LEXINGTON

SECURITIES AND
EXCHANGE COMMISSION, ... Plaintiff,

v.

AMERICAN ASSOCIATED
SYSTEMS, INC.,
BELVA MANOR, INC.,
AMERICAN ASSOCIATED
FINANCIAL CORP.,
JOEL S. JACKSON,
ALVIN L. NORTON,
WILLIAM E. BOHON,
PAUL D. ROSS,
ROBERT E. LEE,
MAJO. GEN. BENJAMIN J. BUTLER,
DR. CHARLES N. TARKINGTON,
MAXWELL B. DUNCAN, SR., ... Defendants.

CIVIL ACTION
FILE NO. 2243
Filed July 31, 1972

FINAL JUDGMENT OF PERMANENT INJUNCTION AGAINST ROBERT E. LEE

This cause coming on to be heard on motion of Plaintiff, Securities and Exchange Commission, for a Final Judgment of Permanent Injunction in accordance with the complaint filed herewith as to the defendant Robert E. Lee, and it appearing to the Court that it has jurisdiction of the parties hereto and the subject matter hereof and the Court having heard evidence and arguments of counsel and the Court having adopted findings of fact and conclusions of law, and now being fully advised in the premises:

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED:

1. That the defendant, Robert E. Lee, his agents, servants, attorneys, employees, and each of them, be and hereby are restrained and permanently enjoined from directly or indirectly, in the offer or sale of common stock of Belva Manor, Inc., or any other security, by use of the mails or any means or instrumentalities of transportation or communication in interstate commerce, employing devices, schemes or artifices to defraud, obtaining money or property by means of untrue statements of material facts or omitting to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or engaging in any act or practice, or course of business which would

operate as a fraud or deceit upon purchasers of such securities.

2. That the defendant, Robert E. Lee, his agents, servants, attorneys, employees and each of them, be and hereby are restrained and permanently enjoined from directly or indirectly, in the offer or sale of common stock of American Associated Financial Corporation, or any other security, by use of the mails or any means or instrumentalities of transportation or communication in interstate commerce, employing devices, schemes, or artifices to defraud, obtaining money or property by means of untrue statements of material facts, or omitting to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or engaging in any act or practice, or course of business which would operate as a fraud or deceit upon purchasers of such securities.

3. That the defendant, Robert E. Lee, his agents, servants, attorneys, employees, and each of them, be and hereby are restrained and permanently enjoined from directly or indirectly, in connection with the purchase or sale of the common stock of Belva Manor, Inc., American Associated Financial Corporation, or any other security, by use of the means and instrumentalities of interstate commerce or of the mails, employing any device, scheme or artifice to defraud, engaging in acts, practices or a course of business which would operate as a fraud or deceit upon any person or making untrue statements of material facts or omitting to state material facts necessary in order

to make the statements made, in the light of the circumstances under which they were made, not misleading.

DATED: Juiy 31, 1972.

ENTER:
/s/ Mac Swinford
United States
District Court Judge

Notice is hereby given of the
entry of this order or judgment
on 7-31-72

Davis T. McGarvey, Clerk
By: /s/ Nancy C. Anderson D. C.

A True Copy Attest
Davis T. McGarvey, Clerk
U. S. District Court
By: /s/ Nancy C. Anderson
D. C.

* * * * * * *

LIBRARY
SUPREME COURT, U. S.

No. 73-699

Supreme Court, U. S.
FILED
NOV 28 1973
MICHAEL RODAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1973

ROBERT E. LEE, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

ROBERT H. BORK,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

LAWRENCE E. NERHEIM,
General Counsel,
Securities and Exchange Commission,
Washington, D.C. 20549

In the Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-699

ROBERT E. LEE, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

Petitioner Lee seeks review of an order permanently enjoining him from further violation of the antifraud provisions of the Securities Act of 1933, 15 U.S.C. 77a, *et seq.*, and the Secutities Exchange Act of 1934, 15 U.S.C. 78a, *et seq.*

Petitioner was enjoined by the United States District Court for the Eastern District of Kentucky because of his activities arising out of his relationship with American Associated Systems, Inc. ("American Associated"), and its subsidiaries. While not a named officer or director, Lee was chief corporate counsel of American Associated and a member of its executive committee. He was also a principal of the management company which had as its only client American Associated and its subsidiaries. The courts below found that Lee, in these capacities, had been instrumental in the frauds

of the companies, through his participation in directors' meetings and preparation of false and misleading corporate documents (Pet. App. 1a-3a, 10a-17a).

Through his protestations that he was merely an employee of American Associated without any managerial authority, petitioner in effect urges that this Court should review, *de novo,* the findings of fact of the district court, affirmed by the court of appeals. In its *per curiam* opinion, the latter court stated, "A careful review of the record reveals substantial support for the District Court's findings * * *" (Pet. App. 2a-3a), and appended the district court's findings to its opinion (Pet. App. 3a-9a). Further review is inappropriate, and the petition should be denied. *Graver Mfg. Co.* v. *Linde Co.,* 336 U.S. 271, 275.

Respectfully submitted.

ROBERT H. BORK,
Solicitor General.

LAWRENCE E. NERHEIM,
General Counsel,
Securities and Exchange Commission.

NOVEMBER 1973.

DOJ-1973-11